
OMB FINAL SEQUESTRATION REPORT
TO THE PRESIDENT AND CONGRESS
FOR FISCAL YEAR 2003



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET

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THE DIRECTOR

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

December 6, 2002

The President
The White House
Washington, DC 20500

Dear Mr. President:

Enclosed please find the *OMB Final Sequestration Report to the President and Congress for fiscal year 2003*, as required by the Budget Enforcement Act of 1990 (BEA), as amended. This report provides the status of overall discretionary spending and pay-as-you-go legislation based on Congressional action to date.

The overall discretionary spending caps expired on September 30, 2002. Although category caps still exist for transportation and environmental conservation activities, there currently are no BEA mechanisms in place for their enforcement.

The pay-as-you-go requirement for revenue and mandatory spending legislation also expired at the end of 2002. While the BEA called for OMB to make annual reductions in Medicare, farm programs, student loans, and other programs through 2006 to offset the deficit effects of bills enacted prior to its expiration, the recently enacted P.L. 107-312 effectively repealed this requirement.

Sincerely,

A handwritten signature in blue ink, reading "ME Daniels, Jr.", with a stylized flourish at the end.

Mitchell E. Daniels, Jr.
Director

Enclosure

Identical Letter Sent to The Honorable Richard Cheney
and The Honorable J. Dennis Hastert

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GENERAL NOTES

- 1. All years referred to are fiscal years unless otherwise noted.
- 2. Details in the tables and text may not add to totals due to rounding.

I. OVERVIEW

The Budget Enforcement Act of 1997 (BEA of 1997) requires OMB to issue an end-of-session report after Congress adjourns *sine die* to determine whether or not a sequester is required. The overall discretionary spending caps expired on September 30, 2002. Although category caps still exist for transportation and environmental conservation activities, there currently are no BEA mechanisms

in place for their enforcement. The pay-as-you-go (PAYGO) requirement also expired at the end of 2002. While the BEA called for OMB to follow the PAYGO sequestration process through 2006 for bills enacted prior to its expiration, the recently enacted Public Law 107-312 reset the PAYGO balances for all fiscal years to zero.

II. STATUS OF DISCRETIONARY SPENDING

Discretionary programs are funded annually through the appropriations process. The Budget Enforcement Act (BEA) required that OMB issue reports after enactment of individual appropriations bills on the scoring of those bills and three times a year on the overall status of discretionary legislation. Since the BEA expired on September 30, 2002, along with the overall discretionary caps and the means to enforce those caps, this requirement is no longer in effect. Until alternative budget constraints are established, OMB will continue to issue periodic reports of the costs of such legislation.

The purpose of this section is to provide OMB's estimates of discretionary appropriations action as of November 17, 2002, based on the scorekeeping guidelines accompanying the BEA. The estimates rely on the same economic and technical assumptions as in the President's 2003 Budget, which the Administration transmitted to Congress on February 4, 2002.

Table 1 shows the President's request and OMB scoring of the latest House and Senate action for the 13 annual appropriations bills. Since the Sequestration Update report was transmitted to the Congress on August 19,

2002 the Congress completed action on the Department of Defense and Military Construction Appropriations bills. Resources for the discretionary programs that are normally funded under the 11 remaining appropriations bill are provided under the terms and conditions of Public Law 107-294, the fifth Continuing Resolution that will expire on January 11, 2003.

The Administration continues to support the discretionary spending levels set in the House-passed Budget Resolution (H.Con.Res. 353). Such a total provides for needed resources for national defense during this time of war abroad and homeland security while restraining overall government spending. The Administration has made fiscal discipline a priority. Fiscal discipline and constraints on overall government spending are critical to the Nation's ability to provide needed resources for national priorities and a fiscal environment that encourages continued economic growth. An extension of the BEA at levels that restrain discretionary growth rates is an important means to ensure this fiscal discipline. The Administration looks forward to working with the Congress in the next session to reform the budget process in a way that meets these important goals.

Table 1. STATUS OF 2003 APPROPRIATIONS ACTION
(In millions of dollars)

	Request		House		Senate	
	BA	Outlays	BA	Outlays	BA	Outlays
TOTAL DISCRETIONARY						
Agriculture and Rural Development	17.1	17.6	17.7	17.7	18.0	18.0
Commerce, Justice, State and the Judiciary	40.4	43.6	40.3	43.0	43.2	44.0
Defense	356.6	342.2 ¹	354.9	339.3	354.9	339.3
District of Columbia	0.4	0.4	0.5	0.5	0.5	0.5
Energy and Water Development	25.5	25.4	26.0	25.7	26.3	28.9
Foreign Operations	16.5	16.5	16.6	16.3	16.4	16.3
Interior and Related Agencies	18.9	19.4	19.7	19.9	19.3	19.7
Labor, HHS, and Education	130.6	123.9 ²	130.9	125.8	134.5	125.6
Legislative	3.4	3.6	3.4	3.5	3.4	3.6
Military Construction	9.5	10.2	10.5	10.0	10.5	10.0
Transportation and Related Agencies	19.4	56.4	19.8	57.8	20.2	59.1
Mass Transit BA (non-add)	1.4	.....³	1.4	C ³	1.5	.....
Treasury, Postal Service, and General Government	18.0	17.7	18.5	17.9	18.5	18.1
Veterans Affairs, HUD, Independent Agencies	92.2	98.1	90.8	97.7	92.8	98.1
Allowances/Unallocated	0.5	7.4	.....	0.7	10.1	13.4
Subtotal, Discretionary Spending, excluding P.L. 107-206.	749.1	782.5	749.7	776.0	768.5	794.4
Total, 2003 effects of the 2002 Supplemental Appropriations Act, P.L. 107-206 .....	.....	9.8	.....	9.8	.....	9.8
Total, Discretionary Spending	749.1	792.3	749.7	785.8	768.5	804.2

Key: S = Subcommittee-Reported bill; C = Committee-Reported bill; F = Bill Passed by House or by Senate; CN = Conference Action has Occurred; E = Enacted bill; A = latest 302(b) allocation.

Note: OMB scoring of latest House and Senate action is preliminary.

¹The Administration's request for Defense excludes a \$10 billion reserve for the war on terrorism.

²Estimates include BA and associated outlays for Adoption Incentive Payments. The House 302(b) allocation included a \$1 billion reserve the House Resolution created for special education programs (IDEA), which is included in the amount shown above.

³The Mass Transit BA is not included in any of the discretionary totals. Therefore, it is displayed here as a non-add line.

III. PAY-AS-YOU-GO SEQUESTRATION REPORT

The PAYGO requirement applies only to direct spending and receipts legislation enacted through September 30, 2002. However, the PAYGO sequestration process continues through September 30, 2006 for the outyear effects of legislation enacted prior to October 1, 2002.

The BEA defines direct spending as entitlement authority, the food stamp program, and budget authority provided by law other than in appropriations acts. The BEA exempts the following from the PAYGO scorecard: Social Security, the Postal Service, legislation specifically designated as an emergency requirement, and legislation fully funding the Federal Government's commitment to protect insured deposits.

The BEA requires that, in total, receipts and direct spending legislation not result in a net cost. If such legislation yields a net cost, and if the President and Congress do not fully offset it by other legislative savings, the law requires that a sequester of non-exempt direct spending programs offset the net cost.

The BEA requires that OMB submit a report to Congress that estimates the resulting change in outlays or receipts for the current year, the budget year, and the following

four fiscal years for enacted direct spending and receipts legislation. The estimates, which must rely on the economic and technical assumptions underlying the most recent President's budget, determine whether the PAYGO requirement is met. The PAYGO process requires that OMB maintain a "scorecard" that shows the cumulative net cost of such legislation.

Table 2 presents OMB estimates of PAYGO legislation enacted as of September 30, 2002, included in the individual bill reports. Since the Balanced Budget Act of 1997, these bills have resulted in net costs of \$2.3 billion in 2002 and \$125.1 billion in 2003 in total. As required by the BEA, the 2002 total reflects only Acts added to the scorecard after the 2002 final sequestration report was issued. Under the BEA, the 2002 and 2003 totals are combined when determining the need for sequestration. A combined balance of \$127.4 billion was on the PAYGO scorecard for 2003 prior to the adjustment required by Public Law 107-312 to reduce preexisting PAYGO balances. Because that Act reset the balances for all fiscal years to zero, no mandatory sequester is required for 2003 and the following years. The table also shows the CBO estimate for each Act as it was reported in CBO's PAYGO bill reports.

Table 2. NET COST OF PAY-AS-YOU-GO LEGISLATION ENACTED AS OF SEPTEMBER 30, 2002¹
(In millions of dollars)

Report Number	Act Number	Act Title	2002	2003	2004	2005	2006	2002-2006
Legislation enacted since the Balanced Budget Act of 1997:								
Balances shown in 2003 Preview Report (also 2002 End-of-Session report)								
		OMB estimate		110,694	129,857	130,571	134,698	505,820
		CBO estimate		109,985	127,476	126,507	139,310	503,278
Legislation enacted in the 2nd session of the 107th Congress as of Sept. 30, 2002:								
574	P.L. 107-139 S. 1762	Student Loan Interest Rate Amendments						
		OMB estimate	-180	345	875	1,005	995	3,040
		CBO estimate	-180	345	875	1,005	995	3,040
575	P.L. 107-138 H.R. 1913	Acoma Indian Ownership Rights						
		OMB estimate		2				2
		CBO estimate		2				2
576	P.L. 107-147 H.R. 3090	Job Creation and Worker Assistance Act ²						
		OMB estimate	46,538	36,878	29,022	-3,001	-20,714	88,723
		CBO estimate	50,869	42,932	29,098	3,571	-16,115	110,355
577	P.L. 107-171 H.R. 2646	Farm Security and Rural Investment Act of 2002						
		OMB estimate	2,384	10,195	11,453	11,065	9,924	45,021
		CBO estimate	1,613	8,406	9,854	10,212	9,867	39,952
578	P.L. 107-181 H.R. 4156	Clergy Housing Allowances Clarification Act						
		OMB estimate	-*	-1	-2	-2	-2	-7
		CBO estimate			-1	-1	-2	-4
579	P.L. 107-195 H.R. 4560	Spectrum Auction Reform Act						
		OMB estimate		2,150	3,150	-3,900	-3,850	-2,450
		CBO estimate		775	1,300	1,525	-2,200	1,400
580	P.L. 107-196 S.2431	Mychal Judge Police and Fire Chaplains Public Safety Officers' Benefit Act						
		OMB estimate	2	*	*	*	*	2
		CBO estimate	2	*	*	*	*	2
581	P.L.107-188 H.R. 3448	Public Health Security and Bioterrorism Preparedness and Response Act						
		OMB estimate		*	*	*	*	*
		CBO estimate		1	1	1	1	4
582	P.L.107-204 H.R. 3763	Sarbanes-Oxley Act of 2002						
		OMB estimate		-7	-5			-12
		CBO estimate		-7	-5			-12
n/a	P.L.107-206 H.R. 4775	2002 Supplemental Appropriations Act						
		OMB estimate						
		CBO estimate						
583	P.L.107-210 H.R. 3009	Trade Act						
		OMB estimate						
		CBO estimate						
584	P.L.107-228 H.R. 1646	Foreign Relations Authorization Act for FY 2003						
		OMB estimate		5	8	8	9	30
		CBO estimate		264	14	14	15	307

OMB does not consider this bill as subject to pay-as-you-go.

Table 2. NET COST OF PAY-AS-YOU-GO LEGISLATION ENACTED AS OF SEPTEMBER 30, 2002¹—
Continued
(In millions of dollars)

Report Number	Act Number	Act Title	2002	2003	2004	2005	2006	2002–2006
585	P.L.107–229 H.J.Res. 111	Making Continuing Appropriations						
		OMB estimate		162	15	14	5	197
		CBO estimate		94	31	22	8	155
		Subtotal, legislation enacted in the 2nd session of the 107th Congress as of Sept. 30, 2002 (including emergency):						
		OMB estimate	48,858	51,250	46,105	8,056	–11,673	142,597
		CBO estimate	52,744	53,853	42,593	17,918	–5,804	161,304
		Remove amounts designated as emergency:						
		Job Creation and Worker Assistance Act ²						
		OMB estimate	–46,538	–36,878	–29,022	3,001	20,714	–88,723
		CBO estimate	–50,869	–42,932	–29,098	–3,571	16,115	–110,355
		Subtotal, legislation enacted in the 2nd session of the 107th Congress as of Sept. 30, 2002 (excluding emergency):						
		OMB estimate	2,320	14,372	17,083	11,057	9,041	53,874
		CBO estimate	1,875	10,921	13,495	14,347	10,311	50,949
		Total, legislation enacted since the Balanced Budget Act of 1997:						
		OMB estimate	2,320	125,066	146,940	141,628	143,739	559,694
		CBO estimate	1,875	120,906	140,971	140,854	149,621	554,227
		Remove balances pursuant to P.L. 107–312:						
		OMB estimate	–2,320	–125,066	–146,940	–141,628	–143,739	–559,694
		CBO estimate	–1,875	–120,906	–140,971	–140,854	–149,621	–554,227
		Current balances:						
		OMB estimate						
		CBO estimate						

* \$500,000 or less.

¹ Excludes bills with impact of \$500,000 or less in each fiscal year 2002 through 2006 under both OMB and CBO scoring.

² This Act was designated as emergency and therefore, is exempt from the pay-as-you-go scorecard.

Table 3. PAY-AS-YOU-GO LEGISLATION WITH IMPACT OF \$500,000 OR LESS ENACTED IN THE 2ND SESSION OF THE 107TH CONGRESS AS OF SEPTEMBER 30, 2002

(paygo reports not issued for these bills)

Public Law Number	Act Number	Act Title
P.L. 107-122	S. 1793	Higher Education Relief Opportunities for Students Act
P.L. 107-150	H.R. 1892	Family Sponsor Immigration Act
P.L. 107-153	S. 1857 ¹	To encourage the negotiated settlement of tribal claims
P.L. 107-155	H.R. 2356	Bipartisan Campaign Reform Act
P.L. 107-170	H.R. 4167	Family Farmer Bankruptcy Extension Act
P.L. 107-173	H.R. 3525	Enhanced Border Security and Visa Entry Reform Act
P.L. 107-174	H.R. 169	Notification and Federal Employee Antidiscrimination and Retaliation Act of 2002
P.L. 107-185	H.R. 1840	To Extend Eligibility for Refugee Status to Unmarried Sons and Daughters of Certain Vietnamese Refugees
P.L. 107-197	H.R. 3275	To Implement the International Convention for the Suppression of Terrorist Bombings and for other purposes
P.L. 107-201	S. 2594	Support of American Eagle Silver Bullion Program Act
P.L. 107-202	H.R. 2362	Benjamin Franklin Tercentenary Commission Act
P.L. 107-205	H.R. 3487 ¹	Nurse Reinvestment Act
P.L. 107-207	H.R. 2175	Born-Alive Infants Protection Act
P.L. 107-208	H.R. 1209	Child Status Protection Act
P.L. 107-216	H.R. 1576 ¹	James Peak Wilderness and Protection Area Act
P.L. 107-223	H.R. 3380 ¹	An act to authorize the Secretary of the Interior to issue right-of-way permits for natural gas pipelines within the boundary of Great Smoky Mountains National Park
P.L. 107-226	H.R. 3917	Flight 93 National Memorial Act

¹ OMB does not consider this bill as subject to pay-as-you-go requirements; CBO does.

Comparison with CBO Estimates.—The BEA requires that OMB explain differences with CBO estimates of enacted PAYGO legislation. For legislation enacted in the 2nd session of the 107th Congress as of September 30, 2002, OMB estimates a net cost of \$142.6 billion over five years, while CBO estimates a net cost of \$161.3 billion for the same period. OMB's estimate is \$18.7 billion lower than CBO largely due to scoring differences in pricing of the Job Creation and Worker Assistance Act. The differences largely result from different revenue baselines and estimating models. However, the cost estimates for this bill are not retained on the PAYGO scorecard, because they were designated as an emergency requirement, which is exempt from the BEA. Excluding this emergency requirement, OMB's cost estimate is \$2.9 billion higher than CBO largely due to scoring differences for the Farm Security and Rural Investment Act, the Trade Act, and the Spectrum Auction Reform Act.

OMB's cost estimate for the Farm Act is \$5.1 billion higher than CBO largely due to differing assumptions about prices

and loan rates for farm income support payments to producers. OMB's estimate for the Trade Act is also \$2.2 billion higher than CBO due to estimates of the revenue impact of the trade and health insurance provisions and outlay impact of the Trade Adjustment Assistance (TAA) expansions. These differences result from different revenue baseline and estimating models and different assumptions about TAA spending and participation rates and the anticipated growth in weekly trade benefits. OMB's higher cost estimates for the farm and trade bills are partially offset by its lower estimate for the Spectrum Auction Reform Act. OMB's cost estimate for this Act is \$3.9 billion lower than CBO due to different assumptions about baseline receipts, the timing of rescheduled auctions, and the increase in value of the spectrum resulting from delay.

Major Mandatory Changes after the Expiration of the BEA.—Table 4 presents OMB estimates of major mandatory provisions enacted or cleared by the Congress after the BEA expired. OMB estimates the major provisions

total \$1.7 billion over the 2004 through 2006 period. The Bob Stump National Defense Authorization Act authorized a special compensation payment for uniformed services retirees who completed at least 20 years of service creditable for retirement and incurred a qualifying combat-related disability. These benefit payments are to be paid out of military pay and allowances accounts. Because the annual pay and allowances appropriations for 2003 were enacted prior to the authorization, OMB estimates the new benefit payments would be offset by lower discretionary spending in 2003, resulting in net zero cost. The Type 1 Diabetes Program Authorization Act appropriated \$0.3 billion for each of fiscal years 2004 through 2008 for special diabetes research.

As noted on Table 4, even though the Terrorism Risk Protection Act could potentially have a significant cost, OMB cannot estimate the timing or the magnitude of the cost, because it cannot predict how much insured damage terrorists might cause in the future. CBO cannot predict the cost for the same reason, but it does provide an estimate based on an expected value of payments from the program. The expected value is a weighted average reflecting the probabilities of various outcomes due to possible future terrorist attacks. On this basis, CBO estimates net costs of \$0.6 billion in 2003 and \$5.0 billion over the 2003 through 2006 period.

Table 4. MAJOR MANDATORY CHANGES ENACTED OR CLEARED BY THE CONGRESS AFTER THE EXPIRATION OF THE BEA ¹

(In millions of dollars)

	2002	2003	2004	2005	2006	2002–06
Special Compensation for Certain Combat-Related Disabled Uniformed Services Retirees (P.L. 107–314, Bob Stump National Defense Authorization Act for FY 2003):						
Preliminary estimate			269	275	280	824
Diabetes Research (H.R. 5738, Type 1 Diabetes Program Authorization Act):						
Preliminary estimate			300	300	300	900
Total, major changes			569	575	580	1,724

¹OMB cannot estimate the mandatory cost of providing financial assistance to commercial property and casualty insurers for losses from certain terrorist acts as required by the Terrorism Risk Protection Act (P.L. 107–297).

IV. PAY-AS-YOU-GO SEQUESTER ISSUES

Although the current PAYGO scorecard balances have been zeroed out, which eliminated the potential PAYGO sequester under the current Budget Enforcement Act provisions, the Administration supports extension of budget controls in the next Congress. In contemplating such action, both the Congress and the Administration might want to consider addressing certain classification and implementation issues for newly enacted programs under the BEA PAYGO sequester provisions.

Section 255 of the BEA provides a list of programs and categories of spending that are exempt from sequester. This listing, along with the general and special rules in section 256, provides the guidance for OMB to implement a sequester. These two sections of BEA have usually been updated whenever the law is amended or extended to take into account relevant legislation enacted during the interim. Since the law was last updated in 1997, a number of direct spending programs have been created. None of the legislation creating these new direct spending programs addressed the issue of whether or how to sequester the new program. Without a specific legislative exemption from sequester, newly created direct spending programs, or those otherwise brought into the budget,

are, by default, subject to sequester unless they happen to fall into one of the few categories of spending that are given categorical exemption. However, several of the new programs that have not been exempted would require special rules if a sequester were to be implemented, and some of the new programs are similar to older programs that were specifically exempted.

The major programs (and FY 2003 outlay amounts) at issue are:

- Refundable portion of the child tax credit (\$7.4 billion)
- Universal Service Fund (\$3.9 billion)
- State children's health insurance fund (SCHIP) (\$4.4 billion)
- September 11th victim compensation fund (\$2.7 billion)
- Air transportation stabilization program account (\$1.5 billion)

OMB recommends that any new or extended budget enforcement legislation specifically address not only the sequester classification and implementation rules for these specific programs, but that it also provide guidelines for treating subsequently enacted programs.